

## Policy faux pas

**The main challenges facing the caretaker government, apart from its fundamental constitutional responsibility of holding a free and fair election, are containing inflation, restoring business confidence (i.e. increasing investment), revamping agricultural production affected by the floods, and creating additional employment opportunities. These are difficult problems to deal with, even at the best of times.**

M.A. TASLIM

**T**HE macroeconomic environment of the country has visibly deteriorated in the recent past. Most of the macroeconomic indicators exhibit the symptoms of a slowing economy. Domestic credit has plummeted and interest rate has risen markedly.

Exports have nose-dived while imports have risen sharply. Economic growth has stalled, perhaps much more than the official growth figure shows, since a large part of the impact of the inappropriate measures and policies during the last fiscal was borne by the unorganised sector which is not adequately accounted for in the national accounts.

The macroeconomic balance built up assiduously over the last decade is in danger of being torn asunder by the relentless upward march of the price level. The overall economic picture is not pretty, and any credible forecast of the future is not very encouraging.

The economy was chugging along reasonably well during the period 2002-05, and there were expectations that it would do even better in the following years. Business confidence was

high and investment was booming. Capital machinery imports had leaped up by 54 percent in 2004-05 after increasing by more than 33 percent in 2003-04. But this business optimism was shattered by the Bangladesh Bank's decision to impose a tight monetary policy.

The very announcement of its desire to raise the interest rate signaled to the market that the economy would soon cool off. It generated fears of difficult times ahead. The business sector responded by cutting back on investment. Total capital imports remained virtually stagnant during the following two fiscal years.

The slowdown in investment had the expected impact on employment and income through a multiplier process. The employment indices of almost all industries reported by BBS Monthly Bulletin show virtual stagnation in employment. This deprived workers of the normal increase in real wages.

After continuously increasing since the beginning of the new millennium, the real wage became flat after 2004-05, and might have even declined in the recent months. The woes of the ordinary working people have

truly begun.

Worse was still to come. During the next fiscal year (2006-07) the nation was hit by, to quote an advisor of the caretaker government, a political tsunami. Its impact was also felt by the economy, which was already smarting from the effects of the tight monetary policy. Other inappropriate policies and ill-conceived market interventions brought on a slump in economic activities and gave a further boost to the spiraling inflation which appears to be moving out of control.

The inflation, especially the double-digit food price inflation, has a particularly severe impact on the poorer section of the population who spend the major part of their income on food.

Inflation has been creeping up gradually since the beginning of the millennium; however, it is the large increase in food prices during the last few years that has aggrieved the people most. When the price of edible oil rose sharply in 2003, there was a chorus of protests. Just about everyone, including the think-tanks, blamed it on syndication and hoarding. Since then every bout of increase in the prices of essentials has been alleged to be

the evil work of some dark syndicates.

This entirely unsubstantiated theory (allegation) inexplicably found favour with the new administration. It went after the business community with a revolutionary zeal to prevent what it thought was hoarding. It is interesting that the business people on whom the axe fell were not told what they were being accused of, which would have required some analytical work to find a legal definition of hoarding.

In the absence of such a definition, whatever the law enforcers on the ground regarded as hoarding became hoarding, regardless of the legality or economics of the matter. The harassment that ensued had the expected result -- the business people reduced the scale of their activities. The consequent market disruptions added fuel to the fire of inflation.

It is not easy to provide an operational definition of hoarding. All businesses must hold stocks of the goods they sell. They also hold stocks of intermediate goods and raw materials as an essential part of the production processes. In economics and business, such stocks are called inventories. Inventories are regarded as investment in macroeconomics and national income accounting in recognition of the fact that inventories are essential for smooth and uninterrupted production and delivery of goods and services.

The amount of inventories that any particular business

enterprise should hold depends on a host of factors, including the characteristics of the good being sold/produced, and the goods held in inventories, the size and other characteristics of the enterprise, technology, risks and attitude toward risks, interest rates, current prices, and prices expected to prevail in the future. The inventory requirement of a kalijira rice trader is not quite the same as that of an ordinary rice trader or a fresh fish seller.

Each business must work out its own optimal level of inventories. Even in the same line of business, inventories are likely to differ, depending on the characteristics of the firm.

In its zeal to eliminate hoarding, what the government essentially did, albeit unintentionally, was to prevent the traders from holding the optimal level of inventories. The reduction in inventories must have impaired their capacity to service the market at the normal level. The consequent market disruptions caused prices to rise further.

The drive against hoarding predictably ended up with a large number of distressed business people, discontented consumers, and a frustrated government. Only after this very costly and counterproductive experiment, the government realised the folly of the anti-hoarding drive and apparently abandoned it. It could have avoided having to learn from its own mistakes if it had an adequate understanding of the economics of the market.



Unfortunately, the government seems to have abandoned one egregious theory of price hike only to adopt another. It is now partial to another unsubstantiated theory that middlemen are the real cause of the price spiral. Accordingly, the proverbial middlemen have become the new targets. The law enforcers are now going after the middlemen for selling at high prices and some have been arrested and displayed in the electronic media.

Since most of these middlemen are ordinary people of very limited means we have not witnessed the same degree of outcry as we had witnessed earlier in the case of the drive against hoarding which affected the very

rich and influential people. But its impact, unless called off, will be no less harmful. Prices will rise if the middlemen are prevented from providing intermediate services in the marketing process. Their essential functions will be then performed by people who are less specialised in those activities and will end up costing more.

It is good to remember that if an economic activity or institution exists, there is a very good economic rationale for its existence. Trying to get rid of it without first eliminating the rationale for its existence can only have perverse outcomes.

The main challenges facing the caretaker government, apart from its fundamental constitu-

tional responsibility of holding a free and fair election, are containing inflation, restoring business confidence (i.e. increasing investment), revamping agricultural production affected by the floods, and creating additional employment opportunities. These are difficult problems to deal with, even at the best of times.

Nonetheless, the government must find innovative ways of attaining these objectives. It has bravely accepted a difficult challenge at a crucial moment of our history. It must not let the nation down.

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## The water problem

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**W**ATER means life for the human body, and is the lifeline for any civilisation to take root and flourish. All known civilisations grew around a water source to support life, and to give life to its economy. With change in time, the economic role of water has changed, taking a different but vital facet. But its role in sustaining life, for which there is no substitute, has remained, and turned out to be indispensable because of higher demand from the growing population across the globe.

Arising from the binding need for water, Dhaka, our capital developed, along the Buriganga, Egypt along the Nile, Mesopotamia along the Euphrates and Tigris, London along the Thames, large cities in India along the Ganges, and so on.

In economic terms, any commodity, though crucial for life and existence, supplied in abundance loses its value, as is the case with air, without which humans cannot survive, the unlimited availability of which has moderated its explicit importance. As long as human population was limited, the abundant supply of natural water had masked its apparent importance, but the progressive growth of population

around the world gradually unveiling the demand side increase, with no change in supply, is making water gradually scarcer, and exposing its value in reality.

Despite the fact that more than two-thirds of the Earth's surface is covered with water, 97.5 percent of this is salty, leaving only 2.5 percent as fresh water. Adding to the paradox, only a tiny fraction of the total fresh water resources is available for human use. About 70 percent of the fresh water on the planet is locked up as ice at the poles, and most of the remainder is retained as soil moisture or deposited in deep underground aquifers that are inaccessible to humans.

In the final tally, less than one percent of all the fresh water on earth is technologically and economically accessible for human use.

The UN estimates that people need a minimum of 50 litres of water a day for drinking, washing, cooking and sanitation. Seventy percent of the water used worldwide is for agriculture. Much more will be needed if we are to feed the world's growing population -- predicted to rise from about six billion today to 8.9 billion by 2050.

Therefore, if we go on as we are, millions more will go to bed hun-

gry and thirsty each night than do so already. Today, one person in five across the world has no access to safe drinking water, and one in two lacks safe sanitation. Today, and every day, more than 30,000 children die before reaching their fifth birthday, killed either by hunger or by easily preventable diseases, and adequate safe water is key to good health and a proper diet.

There are several reasons for the water crisis. One is the rise in population and the desire for better living standards. Another is the inefficiency in the way we use much of the water. When a person needs 4 to 5 gallons of water per day to survive, the average American uses 100 to 176 gallons of water each day.

The amount of water needed to grow our food is staggering. To grow a kg. of rice takes between 2000 and 5000 litres, 20,000 litres to fill a kg. jar of coffee, up to 4000 litres to grow the fodder that will deliver a litre of cow's milk, 5000 litres for a kg. of cheese; and up to 11,000 litres to make a quarter-pound hamburger.

Irrigation causes wastage on a prodigious scale, with the water trickling away or simply evaporating before it can do any good, and pollution is making more of the water that is available to us unfit for use. Water withdrawals for irrigation represent 66 % of the total withdrawals and up to 90 % in arid regions, the other 34 % being used by domestic households (10 %), industry (20 %), or evaporated from reservoirs (4 %) (Shiklomanov, 1999).

As groundwater is exploited, water tables in parts of China, India, West Asia, the former Soviet Union and the western United States are dropping -- in India by as much as 3m a year in 1999.

While the world's population tripled in the 20th century, the use of renewable water resources has grown six-fold. Within the next fifty years, the world population will increase by another 40 to 50 %. This population growth -- coupled with industrialisation and urbanisation -- will result in an increasing demand for water and will have serious consequences on the environment.

The emerging water crisis endangers every aspect of human society -- economic, social, ecological, and political. A United Nations report predicts that access to water may be the single biggest cause of conflict and war in Africa in the next 25 years. Such wars are most likely to be in

regions where rivers or lakes are shared by more than one country.

There is already fierce national competition over water for irrigation and power generation -- most notably in the Nile river basin. Cairo warned in 1991 that it was ready to use force to protect its access to waters of the Nile, which also runs through Ethiopia and Sudan.

Water is the most precious resource in the Middle East, more important even than oil. Competition for water from the river Jordan was a major cause of the 1967 war. As populations increase, water becomes scarcer, aggravating regional tensions. The Lebanese have long accused Israel of manipulation of the waters of the River Litani, and Syria accuses it of being reluctant to withdraw from the banks of the Sea of Galilee, the source of up to 30% of Israel's water.

Israelis in the West Bank use four times as much water as their Palestinian neighbours. India has been in dispute with Pakistan over the Indus and with Bangladesh over the Ganges. Over 260 river basins are shared by two or more countries. As the resource is becoming scarce, tensions among different users may intensify, both at the national and international level. In the absence of strong institutions and agreements, changes within a basin can lead to trans-boundary tensions.

The world's supply of fresh water is running out. For much of the world, at least no longer tell the truth. Today, dozens of the planet's greatest rivers run dry long before they reach the sea. They include the Nile in Egypt, the Yellow River in China, the Indus in Pakistan, the Rio Grande and Colorado in the US, the ancient Oxus that once poured into the Aral Sea in Central Asia, the Murray in Australia and the Jordan in the Middle East, which are emptied before they can even reach the countries that bear their names.

The dire state of such rivers is the most visible sign of a profound crisis in how the world uses its water -- a crisis that reflects water's new place as one of the most important and threatened commodities. Unless a timely measure is taken, a global crisis is imminent, leading to a situation that could herald a world in which wars will be fought for dominance over water.

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MICHAEL HIRSH

**T**O get something in this world, you've got to give something," Chris Hill told reporters on Wednesday. That pretty much sums up why Hill, a veteran State Department negotiator and no ideologue, may be on the verge of achieving the Bush administration's biggest diplomatic success to date.

Almost exactly a year after North Korea rolled all of Asia by testing a nuclear device, Hill led a team that managed to extract a pledge from Pyongyang to disable the country's nuclear facilities at Yongbyon (including its plutonium-reprocessing and fuel-rod fabrication plants) by Dec. 31.

Pyeongyang also committed itself to revealing all its nuclear programs by that date and pledging not to proliferate to other countries. In return North Korea will get 950,000 tons of heavy fuel oil and, just as important to Kim Jong Il, the prospect of having his country removed from the US list of terror-supporting states and "normalising" its relations with Washington.

Sounds like a fairly routine negotiation. Except that for the Bush administration this kind of pragmatic tit-for-tat talking with the enemy has been anything but routine. Indeed, a year ago, when North Korea tested and its vice minister of foreign affairs, Kim Gye Gwan, huffed that "we are a nuclear power," such a negotiation would have been all but impossible.

The hard-liners in the administration still had the upper hand -- among them UN ambassador John Bolton and counter-proliferation chief Bob Joseph. Both are now gone from office, and private citizen Bolton in particular is unhappy about the deal Hill made.

"This is classic State Department zeal for the deal," Bolton snapped recently, proceeding to compare Chris Hill to a criminal. "You know, it reminds me of John Erlichman's comment about the Watergate cover-up: save the plan, whatever it takes." The difference this time is that Bolton said that as an outsider on Fox News, to little effect, rather than working to quietly torpedo the agreement, as he certainly would have if he were still Dick Cheney's man on the inside.

The real difference is one of attitude: A willingness to give

even an evil tin-pot dictator like Kim Jong Il something he can take away from the table. In his case, it seems to be mostly respect that Kim is looking for.

That he can never have, but in an effort to avoid war and the horrors of nuclear proliferation -- the plutonium reactor "was churning stuff out into just a couple of months ago," Hill noted -- it may just be worth it to pretend. To grit one's teeth, normalise relations and live with his odious regime a little longer.

Yes, what Kim is doing may amount to "nuclear blackmail," as the Bush administration once called it. But it's not as if this negotiation is going to set a precedent for every other rogue nation; it took North Korea 50 years and hundreds of millions of dollars to build the popgun nuke it detonated last October.

Indeed, it is worth noting that the administration's only other signal diplomatic success -- getting Libya's Muammar Kaddafi to give up his nuclear program in 2003 -- also came about because inflexible ideologues like Bolton were temporarily sidelined. The Libya agreement went forward only after the British, who took the real lead in the negotiations, insisted to the White House that Bolton be barred from the talks.

Bolton, who was then US undersecretary of state for arms control, had wanted to add Libya to the "axis of evil," but Jack Straw, British foreign secretary at the time, and David Manning, a top adviser to then-Prime Minister Tony Blair, prevailed on then-national security adviser Condoleezza Rice and Secretary of State Colin Powell not to do so.

Bolton also refused to reassure Tripoli that the United States did not intend regime change; in other words, he sought to take essentially the same uncompromising tack the administration is now pursuing with Iran (and no longer with North Korea).

The British again resisted, and the White House, which was then (as now) consumed with Iraq, didn't care enough to defy Blair. A deal was struck only after Kaddafi was reassured that Bush would settle for "policy change": surrendering his WMD.

Yet in a confrontation of potentially far greater significance -- with Iran -- the Bush administration isn't looking hard enough for a negotiated way out. Bush's reluctance to fully engage in broad-based



US might wish to apply North Korea lessons to Iran.

diplomacy with Iran -- while permitting talks on narrow issues of practical mutual interest, like Iraq -- stems from his unwillingness to accept the idea that the regime may be here to stay for a long while.

"I think he does believe the Iranian government is fundamentally illegitimate," says Hilary Mann, the Iran director for the National Security Council in Bush's first term.

Hence Washington's talks with Tehran remain half-hearted and artificially broken up into different pieces -- with one set of talks strictly over Iraq and another over nukes (led by the Europeans) -- despite numerous signals from Iranian moderates and pragmatists that things would move along better if there were full engagement.

Even the lead European negotiator, Javier Solana, has said publicly that broader talks, with a far more engaged US (which is the only real threat to Tehran, after all, the Europeans certainly are not), would probably be more successful. Instead Bush continues to fund ineffectual programs targeted at the government.

Today there are back channels (like the one led by former UN ambassador Tom Pickering) and side channels (like the one being conducted by US ambassador to Iraq Ryan Crocker). What we don't have is a senior US envoy

who can put all the issues on the table with Tehran at the same time. The Iranians were once willing to do this.

In 2003 Tehran's diplomats approved a negotiating agenda that would have addressed all the main outstanding issues of interest to Washington -- including Iran's nuclear program, its support for Hizbullah and Hamas and terrorism in general, stabilising Iraq, and a "two-state approach" to the Israeli-Palestinian issue. It was ignored by the White House.

At that time Tehran was operating maybe 20 centrifuges. Now it is running about 3,000 of them. The meagre diplomacy now underway is all but doomed to fail -- the Western powers are edging fitfully toward yet another UN resolution -- and we seem to be heading toward a grim crossroads: either we let Iran have nukes or we go to war.

A third way must be found, and only Washington can create it. Iran, a far larger, more powerful and more sophisticated country than North Korea, is going to demand a lot more than Kim Jong Il -- including some face-saving element of its uranium enrichment program. But we really won't know what Tehran will settle for until we start truly negotiating with it.

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